VZCZCXRO6666
RR RUEHLMC
DE RUEHLM #0370/01 0651005
ZNR UUUUU ZZH
R 061005Z MAR 07
FM AMEMBASSY COLOMBO
TO RUEHC/SECSTATE WASHDC 5582
INFO RUCPDOC/USDOC WASHDC
RUEHGV/USMISSION GENEVA 1861
RUEHNE/AMEMBASSY NEW DELHI 0711
RUEHKA/AMEMBASSY DHAKA 9938
RUEHIL/AMEMBASSY ISLAMABAD 6903
RUEHKT/AMEMBASSY KATHMANDU 4976
RUEHKP/AMCONSUL KARACHI 2151
RUEHCG/AMCONSUL CHENNAI 7475
RUEHGV/USMISSION GENEVA 1862
RUEATRS/DEPT OF TREASURY WASHDC
RUEHLMC/MILLENNIUM CHALLENGE CORPORATION

UNCLAS SECTION 01 OF 02 COLOMBO 000370

SIPDIS

SIPDIS

STATE FOR SCA/INS AND EB/TPP

MCC FOR S GROFF, D NASSIRY AND E BURKE

STATE AND GENEVA PLEASE PASS TO USTR

E.O 12958: N/A
TAGS: ECON ETRD CE
SUBJECT: SRI LANKA: PARA-TARIFFS BOOST REVENUE AND INCREASE PROTECTION

REF: A) 2006 COLOMBO 2070, B) 2006 COLOMBO 2096

¶1. Summary: Tariffs and para-tariffs have hiked Sri Lanka's effective tariff rates to 50-85 percent. The para-tariffs include at least seven different levies, taxes, and surcharges, the rates of which frequently change (generally upward). These fees have added complexity and unpredictability to foreign exporters' and local importers' cost calculations, inhibiting trade and raising consumer costs. Sri Lanka is unlikely to reduce either its tariffs or para-tariffs soon, as it depends on them for income and to protect some local industries. End summary

¶2. Since 2004, Sri Lanka's effective tariff structure has moved steeply upwards. Traditionally, tariffs have been Sri Lanka's main trade policy instrument and a key source of revenue. In addition, Sri Lanka has imposed numerous para-tariffs in the last few years. Many of these are structured as cascading taxes, i.e. taxes applied on already taxed values, which sharply increase final import costs. Affected products include meat, fruits and vegetables; processed/packaged food; chemicals; apparel and linen; personal care products; jewelry; consumer electronics; ceramic ware; kitchen ware; building material; electronics; and motor vehicles.

IMPORT TARIFF STRUCTURE IS TYPICAL

¶3. Sri Lanka has five tariff bands -- 0, 2.5 percent, 6 percent, 15 percent and 28 percent -- generally applied as follows:

-- Free: Textiles, pharmaceuticals, and medical equipment; inputs for export industries
-- 2.5 percent: Basic raw materials
-- 6 percent: Semi-processed raw materials
-- 15 percent: Intermediate products
-- 28 percent: Most finished products

PARA-TARIFFS REALLY ADD UP

¶4. Sri Lanka's array of para-tariffs include the following:

-Export Development Board Cess: Applies to "non-essential" imports.

1-25 percent levy is applied on the Cost plus Insurance plus Freight (C.I.F.) value, plus a 10 percent imputed profit margin.

-Import Duty Surcharge: 10 percent on all dutiable imports.

-Ports and Airports Development Levy (PAL): 3 percent on imports.

-Value Added Tax (VAT): 0 percent, 5 percent, 15 percent, or 20 percent charged on import price, plus 10 percent imputed profit margin plus all taxes.

-Excise Fees: Charged on some products such as aerated water, liquor, beer, motor vehicles, and cigarettes.

-Social Responsibility Levy (SRL): 1 percent surcharge assessed on the import duty to fund the National Action Plan for Children (increased from 0.25 percent on January 1, 2006.)

-Port Handling Charge: Varies by container size.

EFFECTIVE TARIFF RATES HIT 50-80 PERCENT

¶5. Sri Lanka has bilateral free trade agreements with India and Pakistan and participates in the South Asia Free Trade Agreement (SAFTA) with its South Asian Association for Regional Cooperation (SAARC) neighbors. While these agreements fall far short of true free trade agreements, they have reduced the revenue that the Government of Sri Lanka (GSL) derives from tariffs. As a result, the GSL has sought to make up the shortfall through additional levies on imports.

¶6. The following example illustrates the actual tariff plus

para-tariff treatment of a bottle of shampoo imported from the United States, compared to the treatment for shampoo imported from India (both hypothetically priced initially at 100 rupees):

----------------	U.S.	------ India
CIF Value	100.0	100.0
Import Duty	28.0	8.4
Surcharge	2.8	0.8
EDB Cess	27.5	27.5
PAL	3.0	3.0
VAT	25.7	22.5
Excise	na	na
SRL	0.3	0.1
Total cost (a)	187.3	162.3

(a) Does not include port handling charges

¶7. The above example also shows that para-tariffs have a relatively greater impact on trade partners (like the United States) that don't have free trade agreements with Sri Lanka, because the para-tariffs are imposed on the after-tariff value of imports. In this example, para-tariffs on the hypothetical U.S. good enable Sri Lanka to recoup 5.4 percent of the 19.6 percent duty concession that it gives India.

PARA-TARIFFS WON'T BE LOWERED SOON

¶8. Deputy U.S. Trade Representative Karan Bhatia raised Sri Lanka's high tariffs and para-tariffs during bilateral Trade and Investment Framework Agreement (TIFA) talks in December 2006 (ref A). Bhatia noted that the high effective tariffs impede investment and economic reform. The Sri Lankan delegation replied that the GSL intends in the next ten years to move towards tax-driven revenue sources in place of tariffs. Sri Lankan Commerce Department officials have privately acknowledged that the numerous para-tariffs make Sri Lanka's effective tariff rates quite high. But they say that Sri Lanka is unlikely to reduce these duties in the near future, as the

government still depends on border tariffs and para-tariffs for over 40 percent of tax revenue. When Post has raised the high tariffs with Central Bank and government revenue officials, they have admitted that the levies are in place not only to generate revenue but also to protect politically influential domestic producers.

¶9. Comment: When Ambassador met with newly appointed Trade Minster G.L. Peiris in February, he passed the minister a copy of the effective tariff calculations above and noted the discouraging impact such tariffs had on U.S. exports. The minister was surprised to learn that the total tariffs were so high. But with the GSL perennially running a budget deficit, inflation at almost 20 percent, and military spending up (ref B), the only likely change in these para-tariffs is further rate increases or new levies.
3/1/2007